British Columbia Ferry Commission

Annual Report

for the Fiscal Year Ending
March 31, 2014

Prepared and submitted in accordance with
Section 53 of the Coastal Ferry Act
of the Province of British Columbia

British Columbia Ferries Commissioner
PO Box 9279
Victoria, BC V9W 9J7

http://www.bcferrycommission.ca
info@bcferrycommission.ca

Telephone (250) 952-0112

August 31st 2014

To the Lieutenant Governor in Council

Victoria, BC
August 31st, 2014

May It Please Your Honour:

BC Ferry Commission Annual Report
For the Fiscal Year Ending March 31, 2014

I am pleased to submit to you the eleventh Annual Report of the BC Ferries Commissioner.

As required by section 53 of the *Coastal Ferry Act*, the Report sets out briefly all applications and requests for decisions to the Commissioner under the Act, all orders issued by the Commissioner, the financial statements applicable to the Office of the Commissioner for the above period along with full disclosure of the expenses of, and associated with, the Office of the Commissioner.

Yours truly,

Gord Macatee
BC Ferries Commissioner

CONTENTS

Introduction 2
Decisions, Orders and Reports of the Commissioners in 2014 3
BC Ferries and BC Ferry Authority Performance in 2014 6
Price Cap Compliance 7
Activity Summary 8
Financial Statements 9

Introduction

The BC Ferry Commission regulates ferry operators under the *Coastal Ferry Act* of 2003 as amended by subsequent legislation (the "Act"). The Province appoints the commissioner and up to two deputy commissioners for a term of at least six and not more than eight years. They are independent of both the government and the ferry operators. Gord Macatee of Victoria BC was appointed commissioner on May 1, 2011 for a six-year term expiring on April 30, 2017. Sheldon Stoilen of Bowen Island was reappointed deputy commissioner for a six year term expiring on June 30, 2020.

The role of the commissioner is set out in section 38(1) of the Act which stipulates the commissioner must regulate ferry operators in accordance with the following principles:

a) the primary role of the commissioner is to balance, in the manner the commissioner considers appropriate, the interests of ferry users, taxpayers and the financial sustainability of ferry operators;

b) ferry operators are to be encouraged to adopt a commercial approach to ferry service delivery;

c) ferry operators are to be encouraged to seek additional or alternative service providers on designated ferry routes through fair and open competitive processes; and

d) ferry operators are to be encouraged to be innovative and to minimize expenses without adversely affecting their safe compliance with core ferry services.

This is the eleventh annual report of the commissioner and has been prepared in accordance with Section 53 of the Act. The report summarizes all major decisions, orders and reports issued by the commissioner and the financial statements of the Office of the Commissioner for the fiscal year ended March 31, 2014 ("FY 2014"). The report also includes the commissioners' opinion on the performance of British Columbia Ferry Services Inc. ("BC Ferries") relative to its obligations under the Act and the Coastal Ferry Services Contract and the performance of the BC Ferry Authority relative to its obligations under the Act.

Decisions, Orders and Reports of the Commissioners in 2014

The following were the major decisions, orders and reports of the commissioners during FY 2014:

Order 12.02A – April 15, 2013

This Order amends Order 12-02 dated October 1, 2012 and reflects amendments to the Coastal Ferry Services Contract for Performance Term 3 whereby the Province agreed to increase Ferry Transportation Fees by $7.1 million. Accordingly, the aggregate net savings target from service level adjustments used in the determination of price caps for the remainder of Performance Term Three was reduced from $30 million to $22.9 million.

Order 13-01 – July 19, 2013

This Order approved BC Ferries' application under s. 55(2) of the Act for a proposed major capital expenditure for the acquisition of three new diesel-fuelled or liquefied natural gas ("LNG")-fuelled intermediate class vessels subject to the following three conditions:

a) The maximum amount of the major capital expenditure for the three new vessels is set at the amounts stated in the Application which will be confirmed by a separate confidential order to BC Ferries. The maximum amount will remain confidential until completion of the procurement process;

b) Prior to issuing a Request for Proposals for the design and build of the proposed new vessels BC Ferries must satisfy the commissioner that:
   (i) A fuel efficiency target has been included in the technical specifications for the proposed new vessels and reflected in the procurement documents;
   (ii) The concerns of ferry users regarding the open deck design of the new vessels have been taken into account when finalizing the technical specifications for the new vessels and such design will have no significant impact on service levels on the routes where these vessels will be deployed;

c) Prior to signing a final contract with a shipyard for the design and build of the proposed new vessels BC Ferries must:
   (i) Satisfy the commissioner that the actual design of the vessels is as generally as described in the Application and the cost does not exceed the maximum amount approved by the confidential order referred to in paragraph 1(a) above;
   (ii) Obtain the commissioner's approval to select diesel-fuelled vessels rather than LNG-fuelled vessels, and in that event, submit a final comparison of life cycle costs on a net present value basis for the lowest cost diesel-fuelled option and the lowest cost LNG-fuelled option; and
   (iii) Provide the commissioner with a contingency plan to mitigate a delay in the delivery of the new vessels beyond the delivery dates proposed in the Application.

By letter dated June 27, 2014 to BC Ferries, the commissioner confirmed that all of his conditions set out in Order 13-01 had been satisfied.

Order 13.01A – July 19, 2013

This Order approved the maximum amount for the proposed major capital expenditure for the acquisition of three new diesel-fuelled or liquefied natural gas ("LNG")-fuelled intermediate class vessels of:

a) $240.6 million for diesel-fueled vessels: or
b) $274.6 million for liquefied natural gas ("LNG")-fuelled vessels.

Order 14-01 – February 20, 2014

This Order approved BC Ferries' proposed major capital expenditure for the acquisition of a cable ferry and associated infrastructure subject to the following conditions:

1. The maximum amount of the major capital expenditure for the cable ferry and associated infrastructure is set at the amount stated in the Application which will be confirmed by a separate confidential order to BC Ferries. The maximum amount will remain confidential until completion of the procurement process;
2. BC Ferries must advise the commissioner of the actual crewing levels, as finally determined, and confirm that the projected life cycle cost savings will be achieved. If the projected life cycle cost savings are less than the projected savings in the Application the commissioner may not allow the increase in operating costs in future price cap determinations;
3. BC Ferries must satisfy the commissioner that standard operating procedures will be developed and refined as operational experience is gained, to include:
    (a) rigorous inspection, testing and replacement protocol of the cable be put in place with an inspection frequency commensurate with loads experienced at site, and
    (b) operating limits and protocols based on wave conditions that avoid resonant roll by actual measurements of wind speed, wave period and height;
4. Prior to deployment of the cable ferry, BC Ferries must satisfy the commissioner that operational reliability will be assured by:
    (a) enabling a secondary means of recovering vessel from a propulsion system breakdown within a reasonable period of time, and
    (b) maintaining inventory, in the province, of non-redundant parts;
5. At least one vessel on the minor routes will be retired so that the cable ferry does not result in a net increase in the overall size of the fleet.

On March 24, 2014, the BC Ferry and Marine Workers Union filed an application for leave to appeal Order 14-01. The application was dismissed by the BC Court of Appeal on June 27, 2014.

Order 14-01A- February 20, 2014

This Order approved the maximum amount for the proposed major capital expenditure for the acquisition of the new cable ferry and associated infrastructure of up to $41.4 million including interest during construction.

Memorandum 45 – March 20, 2014

This memorandum rejected BC Ferries' proposal for ongoing authority to transfer price cap regulatory account balances to a fuel deferral account for the non-Northern routes. Because of extenuating circumstances the commissioner approved a one-time transfer of the March 31, 2014 balance of tariffs in excess of price cap to reduce the deferred fuel account balance.

Performance Review – 2014

In October 2013, the commissioner engaged the consulting firm of PricewaterhouseCoopers ("PwC") to conduct a performance review on BC Ferries' Automated Customer Experience ("ACE") program. ACE is a complex set of initiatives and new information technologies to improve the customer experience and to better enable customer relationship and demand management.

Based on his review of PwC's report and BC Ferries' responses to the findings and recommendations, the commissioner made the following observations:

1. The ACE program has the potential to enable transformational change in the business model for BC Ferries' by better enabling its revenue generation capabilities and processes;

2. By its very nature, the ACE program has a high risk profile and success will largely depend on an effective governance structure, well-structured project management and delivery functions and effective organizational change management;

3. PwC identified a number of key structural adjustments that should be implemented as the program transitions into the design and delivery phase, as well as a set of leadership recommendations to strengthen project processes and address other risk elements. BC Ferries substantially agreed with all of the findings and has or is in the process of implementing the key recommendations. In considering any project adjustments which may be deemed necessary, BC Ferries should ensure that scope changes will not impair the transformational capability of the ACE program and its fundamental objectives; and

4. By implementing PwC's recommendations, BC Ferries will lower the risk profile for this program by focusing on the key success criteria outlined in (2) above.

BC Ferries and BC Ferry Authority Performance in 2014

During Fiscal 2014 the commissioners continued their practice of conducting quarterly meetings with BC Ferries to review their quarterly reports on price cap compliance, operations summary, customer complaints resolution, and deferral account balances. The commissioners also reviewed and posted on their website BC Ferries' Annual Report to the Commissioners for FY 2014 which was submitted as required before July 31, 2014. The commissioners received satisfactory responses from BC Ferries to all follow-up queries and requests for additional information.

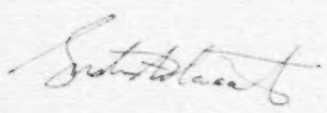
The key findings of the commissioners for the year ended March 31, 2014 are that BC Ferries:

- complied with price cap increase of 4.1% for all routes combined;
- delivered a total of 83,971.5 round trips or 705.5 more than the 83,266.0 round trips required under the Coastal Ferry Services Contract ("CFSC"). Only 12 required round trips (0.01% of total required round trips) were cancelled for reasons other than those specified in Schedule A, 2(a) of the CFSC and were reported to the provincial government;
- maintained good on-time performance of 91.5% system wide and a high standard of service reliability delivering 99.7% of the scheduled sailings;
- provided capacity to carry the traffic with capacity utilization on the designated routes ranging from 23.1% to 72.4% with traffic levels generally flat compared to previous year after adjusting for timing of Easter holiday;
- conducted the annual customer satisfaction survey indicating 87% of passengers in 2013 reported to be satisfied overall with their experience travelling on BC Ferries. These findings were consistent with those recorded in 2012 (88% satisfied); and
- is on pace to achieve cost reductions of $22.9 million from service level adjustments and $54.2 million from efficiency targets incorporated in the price caps for the current performance term.

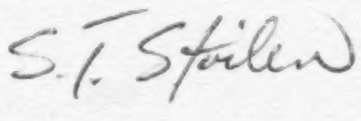
Based on our reviews and key findings, the commissioners are satisfied that during FY 2014, BC Ferries met its obligations under the *Coastal Ferry Act* and also met its obligations under the Coastal Ferry Services Contract.

Finally, based upon a review of BC Ferry Authority's submission to the commissioner and discussion with the Chair of its Board of Directors, the commissioners are satisfied that the BC Ferry Authority performed all of its obligations under the Act during FY 2014.

Gord Macatee
BC Ferries Commissioner



Sheldon Stoilen
Deputy BC Ferries Commissioner



Price Cap Compliance

The chart below tracks the values of the price cap index compared to an index of actual weighted average fares system wide for BC Ferries (price cap index was reset at 100 effective the beginning of the third performance term on April 1, 2012).

The values for the indices are computed by methods laid down in Commission Order 05-01 and Order 11-03 and are based on trailing four-quarter data. The commissioner allows BC Ferries to exceed the price cap (highlighted in colored or shaded text) for no more than three consecutive quarters. This ensures that the company does not retain revenues earned at above-price cap levels.

The chart shows that BC Ferries did not exceed the price cap for more than three quarters during FY 2014. Accordingly, the company was in compliance with the price cap during the year.

BCFerries

Average Fare Index Summary

		PT3 →						
		Sep-2012	Dec-2012	Mar-2013	Jun-2013	Sep-2013	Dec-2013	Mar-2014
System								
	Cap	**102.48**	**103.38**	**104.15**	**105.18**	**106.68**	**107.60**	**108.42**
	Actual	101.78	102.64	103.35	105.80	107.16	108.06	108.42

- Price cap and price compliance indices are calculated in accordance with Commission orders 05-01 and 11-03.

-The annual price cap increase for each fiscal year is phased in over four quarters. The amount phased in will vary from quarter to quarter as it is based on proportions of revenue received in the previous year for that quarter. The amount of the phase in for a particular quarter can vary from year to year due to variations in prior year revenue. Such variations can be caused, for example, by the timing of promotions and changes in the timing of Easter. (Easter occurs in either Quarter 1 or Quarter 4)

-As per BCFC Memorandum 45, BC Ferries has transferred the revenue earned in excess of the price cap to a fuel deferral account, and as a result the Actual index is equal to the Price Cap as at March 31, 2014.

Activity Summary

Commissioner Activities in FY 2014

---

1. **Regulation of Ferry Fares and Service Levels**
   - monitored BC Ferries compliance with the price cap and delivery of contracted round-trips under the CFSC

2. **Special Decisions**
   - adjusted net savings target from service level adjustments from $30 million in PT3 to $22.9 million as a result of an increase of $7.1 million in Transportation Service Fees from the Province
   - approved a major capital expenditure for the acquisition of three new intermediate class vessels for Routes 17 and 9
   - approved a major capital expenditure for a new cable ferry for Route 21, Buckley Bay to Denman Island
   - allowed a transfer of excess revenue to a fuel deferral account for FY 2014

3. **Enforcement and Performance Reviews**
   - conducted a review on the Automated Customer Experience IT project

4. **Administration and Reporting, Publication, Outreach**
   - maintained records; submitted Annual Report and Service Plan; published decisions and communicated with stakeholders

The commissioners' activities during FY 2014 are summarized in the table to the left. The core ongoing activities are **regulating ferry fares** through the price cap mechanism, and **regulating service levels**.

Special decisions include decisions relative to previous orders and the approval of major capital expenditures of which there were two applications under s.55(2) during the year. Special decisions also include consideration of opportunities for possible alternate service providers or the regulation of unfair competitive advantage. There was no activity in these areas during the year other than monitoring compliance with regard to Order 11-01 in respect to drop trailer operations.

There was also no activity in FY 2014 for **enforcement** as BC Ferries was found to be compliance with its obligations under the *Coastal Ferry Act* and the Coastal Ferry Services Contract.

During the year the commissioner conducted a **performance review** on BC Ferries' information technology program referred to as the Automated Customer Experience or "ACE" and reported on the observations and recommendations.

An important activity area is keeping the public informed about the commissioner's role, activities and decisions. The commissioners invited public comments on the proposed major capital expenditures for the three new intermediate class vessels to replace vessels operating on Routes 17 (Comox to Powell River) and Route 9 (Tsawwassen to Southern Gulf Islands) and for the new cable ferry for Route 21 (Buckley Bay to Denman Island). All orders, major decisions and reports were posted on the Commission's website.

Financial Statements

Accounting Services

The Ministry of Justice provides accounting and payment services at no cost to the commission. The summary financial statement is based upon information provided by the ministry.

Summary Financial Statement

BC Ferry Commission
Summary Financial Statement
(Expenditures in $ thousands)

	FY 2014 Budget	FY 2014 Actual	FY 2013 Actual
Commissioners' Fees and Expenses	225	192	232
Professional Services	436	271	100
Other Expenses	6	26	1
	667	**489**	**333**

Budgeted Expenditures

The *Coastal Ferry Act* requires ferry operators to cover the expenses associated with the operation of the Office of the Commissioner. Under section 59(2) of the Act the budget for the Office of the Commissioner must not exceed 1/5 of 1% of the ferry operator's previous year's tariff revenue. Total budgeted expenditures for FY 2014 were $667,000 or 73% of the maximum budget allowable under Act.

Actual Expenditures

Actual expenditures in FY 2014 were $489,000, or 73% of the budget. Expenditures were for commissioners' fees and expenses and for the cost of consultants engaged to assist and advise the commissioners. Professional services were under budget due to timing differences in connection with an anticipated section 55 applications and planned performance reviews.

Commissioners' Remuneration

The commissioner and deputy commissioner are paid a per-diem fee for their services. The commissioner received $71,775 in fees for his services and was reimbursed $3,481 for travel and other expenses. The deputy commissioner received $111,000 in fees for his services and was reimbursed $12,532 for travel and other expenses incurred in the period.